Internal Revenue Service

Department of the Treasury

Washington, DC 20224

200106039

Significant Index No. 72.20-04

Contact Person:

Telephone Number:

In Reference to:

Date: T:EP:RA:T:A2

NOV 14 2000

In re: Request for ruling on behalf of

This letter is in response to your request, dated May 2, 2000, in which you asked for a ruling as to whether certain proposed distributions from an individual retirement account (IRA) owned by you are part of a series of substantially equal periodic payments and are therefore not subject to the 10 percent additional tax imposed under section 72(t) of the Internal Revenue Code (Code). The ruling request was amended by you in telephone calls with of our office on October 23, 2000, and on October 25, 2000, to modify the methodology used to calculate distributions for 2001 and subsequent years.

According to the facts as stated, you retired in 1998 and subsequently received a lump sum distribution of your benefits under your employer's retirement plan, which was rolled over into a traditional IRA (IRA 1). The rolled over amount was divided among a portfolio of different investment accounts administered by the same investment firm, and all accounts are part of IRA 1. Other funds were added to IRA 1 from the rollover (to IRA 1) of the distribution of your benefits under a section 401(k) plan, and from the consolidation of other traditional IRAs owned by you into IRA 1. In addition to IRA 1, you also own a Roth IRA. You attained age 56 in 2000, and your wife attained age 55 in 2000. You decided to start taking distributions from IRA 1 in 2000. You want to avoid the additional 10 percent tax, imposed under section 72(t)(1) on early distributions, by using the exception provided in section 72(t)(2)(A)(iv) of the Code for substantially equal periodic payments. An annual distribution amount for 2000 was calculated by amortizing the total account balance of IRA 1 as of December 31, 1999, over the number of years equal to the joint and last survivor life expectancy for you and your wife, obtained from Table VI of section 1.72-9 of the Income Tax Regulations (as set forth in Table II of IRS Publication 590), using an interest rate of 6.2 percent (the annual short-term applicable federal rate in effect for February 2000. Because monthly distributions first commenced in February 2000, only 11 monthly distributions will be paid in 2000. The annual distribution amount for subsequent years will be calculated using the same methodology, except that the interest rate used will be the annual short-term federal rate in effect for January of the distribution year. That is, an annual distribution amount will be calculated each year by amortizing the account balance of IRA 1 as of December 31

213

of the prior year over the number of years equal to the joint and last survivor life expectancy applicable in the distribution year, using an interest rate equal to the annual short-term applicable federal rate in effect for January of the distribution year. All distributions will be taken from IRA 1.

Ruling Requested

Based on these facts, you have requested the following ruling.

The proposed method of determining periodic payments satisfies one of the methods described in Notice 89-25 and results in substantially equal periodic payments within the meaning of section 72(t)(2)(A)(iv) of the Code, and such payments will not be subject to the additional tax of section 72(t)(1) unless the requirements of section 72(t)(4) are not met.

Applicable Law

Section 408(d) of the Internal Revenue Code provides that amounts paid or distributed out of an individual retirement plan must be included in gross income by the payee or distributee in the manner provided under section 72 of the Code.

Section 72 of the Internal Revenue Code provides rules for determining how amounts received as annuities, endowments, or life insurance contracts and distributions from qualified plans are to be taxed.

Section 72(t) of the Internal Revenue Code was added to the Code by the Tax Reform Act of 1986 (TRA '86), effective generally for taxable years beginning after December 31, 1986. Section 72(t)(1) provides for the imposition of an additional 10 percent tax on early distributions from qualified plans, including IRAs. The additional tax is imposed on that portion of the distribution that is includible in gross income.

Section 72(t)(2)(A)(iv) of the Code provides that section 72(t)(1) shall not apply to distributions which are part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the employee or the joint lives (or joint life expectancies) of such employee and his beneficiary.

Section 72(t)(4) of the Code imposes the additional limitation on distributions excepted from the 10 percent tax by section 72(t)(2)(A)(iv), that if the series of payments is subsequently modified (other than by reason of death or disability) before the later of (1) the close of the 5-year period beginning with the date of the first payment, and (2) the employee's attainment of age 59 1/2, then the taxpayer's tax for the first taxable year in which such modification occurs shall be increased by an amount determined under regulations, equal to the tax that would have been imposed except for the section 72(t)(2)(A)(iv) exception, plus interest for the deferral period.

Section 1.72-9 of the Income Tax Regulations (Regulations) provides tables that are to be used in connection with computations under section 72 and the regulations thereunder. Included in this section are tables giving life expectancies for one life (Table V) and joint life and last survivor expectancies for two lives (Table VI).

Notice 89-25, 1989-1 C.B. 662, provides guidance, in the form of questions and answers, on certain provisions of the Tax Reform Act of 1986 (TRA '86). In the absence of regulations on section 72(t) of the Code, this notice provides guidance with respect to the exception to the tax on premature distributions provided under section 72(t)(2)(A)(iv). Q&A-12 of Notice 89-25 provides three methods for determining substantially equal periodic payments for purposes of section 72(t)(2)(A)(iv) of the Code. Two of these methods involve the use of an interest rate assumption that must be an interest rate that does not exceed a reasonable interest rate on the date payments commence.

Proposed Methodology

The proposed method for determining monthly periodic payments described in the ruling request, as modified, is to calculate an end-of-year annual distribution amount, which is then divided by twelve to obtain a monthly distribution amount. An end-of-year annual distribution amount for 2000 is calculated by amortizing the entire account balance of IRA 1 as of December 31, 1999, over the number of years equal to the joint and last survivor life expectancy for you and your wife, obtained from Table VI of section 1.72-9 of the Income Tax Regulations (set forth in part in Table II of Appendix E in IRS Publication 590) using the ages attained by you and your wife in 2000, using an interest rate of 6.2 percent (the annual short-term applicable federal rate used for purposes of Code section 1274(d), in effect for February 2000). The annual end-of-year distribution amount for 2000 is then divided by 12 to obtain a monthly distribution amount. Because distributions for 2000 commenced in February, only 11 monthly distributions will be paid in 2000. The monthly distribution amount for 2001 will be calculated as one-twelfth of the end-of-year annual distribution amount obtained by amortizing the account balance of IRA 1 as of December 31, 2000, over the number of years equal to the applicable joint life and last survivor expectancy, obtained from Table VI of section 1.72-9 of the regulations (set forth in part in Table II of Appendix E in IRS Publication 590) using the ages attained in 2001 by you and your wife, using an interest rate equal to the annual short-term applicable federal rate (used for purposes of Code section 1274(d)) in effect for January 2001. For subsequent years, the monthly distribution amount will be calculated using the same methodology as that used for 2001. That is, the monthly distribution amount will equal one-twelfth of the annual end-of-year distribution amount calculated by amortizing the account balance of IRA 1, as of December 31 of the prior year, over the number of years equal to the joint and last survivor life expectancy applicable in the distribution year, obtained from Table VI of section 1.72-9 of the regulations (set forth in part in Table II of Appendix E in IRS Publication 590) using the ages attained by you and your wife in the distribution year, using an interest rate equal to the annual short-term applicable federal rate (used for purposes of Code section 1274(d)) in effect for January of the distribution year. All distributions will be taken from IRA 1.

Conclusion

The life expectancy and interest rate used are such that they do not result in the circumvention of the requirements of sections 72(t)(2)(A)(iv) and 72(t)(4) of the Code (through the use of an unreasonable life expectancy or an unreasonably high interest rate).

Accordingly, we conclude that the proposed method (as modified) of determining periodic payments satisfies one of the methods described in Notice 89-25 and results in substantially equal periodic payments within the meaning of section 72(t)(2)(A)(iv) of the Code, and such payments will not be subject to the additional tax of section 72(t) unless the requirements of section 72(t)(4) are not met.

This ruling is directed only to the individual that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

Sincerely yours,

Martin L. Pippins

Martin L. Pippins, Manager
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